

TO: Files

CC: San Diego Audit Committee

FROM: Willkie Farr & Gallagher LLP

RE: Interview of Leslie Devaney on April 18, 2006

DATED: July 6, 2006

On April 18, 2006, Michael Schachter and Michael Shapiro, in Willkie Farr & Gallagher LLP's capacity as counsel to the Audit Committee, interviewed Leslie Devaney at the City Administration Building, 202 C Street, in San Diego, in a conference room on the third floor. Johnny Giang from KPMG also attended the interview. Ms. Devaney was not represented by counsel.

The following memorandum reflects my thoughts, impressions, and opinions regarding our meeting with Leslie Devaney, and constitutes protected attorney work product. It is not, nor is it intended to be, a substantially verbatim record of the interview.

Warnings

Mr. Schachter informed Ms. Devaney that we are counsel to the Audit Committee and do not represent her or any employee. He advised Ms. Devaney that the interview may be considered attorney work product and confidential, but the decision of whether to keep it confidential will be made by the Audit Committee in the best interests of the City, not by Ms. Devaney personally. He said that it is important for Ms. Devaney to keep the contents of the interview confidential to maintain the integrity of the process. Mr. Schachter said that we will create a report which may contain statements of interviewees, and this report will likely be provided to KPMG and ultimately made public. He said government agencies may view the report and be provided with additional information so it is important to be truthful and accurate.

Background

Mr. Schachter asked Ms. Devaney to describe her work background. Ms. Devaney stated that she became an attorney in 1984 and began working for the Office of the City Attorney in 1985 in the Criminal Division. After one year, she transferred to the Civil Division and dealt with cases involving dangerous conditions of roads and police excessive force, from 1985 to 1992. She then left the City's employ to work as Senior Staff Counsel at AIG, which she did for four years until she was asked by City Attorney Casey Gwinn to be Gwinn's second-in-command. She took the post in December 1996. She later ran for City Attorney in October 2003 and lost to Michael Aguirre. In December 2004, she returned to the City Attorney's Office for two months to assist in the transition for Aguirre.

Mr. Schachter asked Ms. Devaney to describe her role and responsibilities. She responded that starting in 1996, she dealt with any issues that had both civil and criminal aspects to them and also dealt with any issues that Gwinn could not or did not want to deal with. She was responsible for the hiring and billing of outside counsel and dealt with "client satisfaction," i.e., improving satisfaction with the City Attorney's Office for the Mayor and Council. She helped reorganize the City Attorney Office and helped decide the personnel makeup of the Gwinn administration. There was a steep learning curve regarding the politics involved. Les Girard, former Assistant City Attorney, is a close friend of hers and assisted her in her tasks.

Mr. Schachter asked Ms. Devaney if she worked on any other issues. Ms. Devaney recalled working on special projects, including an attempt to reverse a \$94 million verdict in a lawsuit lost by the City. She also remembered negotiating on behalf of the City regarding the tobacco settlement. She was also involved in other high impact litigation and made strategic recommendations regarding that litigation.

City Council Closed Sessions

Mr. Schachter asked Ms. Devaney to describe her involvement with City Council Closed Sessions. Ms. Devaney responded that when she first became second-in-command at the City Attorney's Office in 1996, Girard determined what did or did not go into Closed Session. Eventually she made such decisions. She was the "stage manager" for the Closed Sessions and made sure that they were orderly, organized, and efficient. She made sure that all discussion fell within the Closed Session rules. Mr. Schachter asked Ms. Devaney what is or is not appropriate for discussion in Closed Session. She responded that everything should be discussed in Open Session except ongoing litigation, directions to labor union negotiators, real property negotiations, personnel reviews of certain high-level employees, threats to public safety, and actual threats of litigation, not potential litigation threats.

Mr. Schachter asked Ms. Devaney to describe how Closed Session minutes were prepared. She responded that Girard would keep minutes of Closed Session meetings for the meetings he attended. He would fill out a form and provide it to Judy Stone, joint secretary for Girard and Ms. Devaney, who would type up the form. Sometimes Ms. Devaney would sign the form, other times Girard would. If both she and Girard attended, Girard would keep the minutes. Mr. Schachter asked Ms. Devaney what her signature meant on the minutes. She responded that her signature on the minutes meant that the information provided was correct in her opinion and accurately reported what took place. To ensure the accuracy of the minutes, she said that she compared the rough minutes taken by hand at the meeting to the typed minutes to verify that the typed form was correct. Mr. Schachter asked Ms. Devaney what happened to the rough minutes taken by hand. She said she did not know what happened to the rough minutes taken by hand after they were provided to Stone.

Mr. Shapiro asked Ms. Devaney whether she was aware of correspondence between Girard and Councilmember Donna Frye concerning the Cost of Service Study ("COS") being discussed in Closed Session. Ms. Devaney responded that she was unaware of correspondence between Girard and Frye about Closed Session and explained that Girard would not share information and did not delegate. Ms. Devaney and Gwinn relied on Girard for implementing the Brown Act but "the buck stopped" with Gwinn. She deferred to Girard when she first became second-in-command but later questioned his decisions. She said that the COS

should not have been discussed in Closed Session and agreed with Frye on that issue. Girard "would dig in his heels" and take possession of legal issues and make determinations himself.

Bond Disclosures

Mr. Schachter asked Ms. Devaney to discuss her knowledge of bond issues and financings. Ms. Devaney responded that Kelly Salt from the City Attorney's Office was head of the contracts group and worked with Orrick Herrington on bond issues and financings. Disclosure issues were not brought to Devaney's attention, but Salt would ask Devaney to coordinate the deputy attorneys reporting to Anita Noone to obtain disclosures for certain bond disclosure items. Mr. Schachter asked Ms. Devaney if Salt ever asked Devaney for input regarding the bond disclosures. She responded that Salt asked her to provide information regarding the \$94 million judgment in the *De la Fuente* case.

Mr. Giang asked Ms. Devaney if she had any involvement with FAS 5 and letters from the City Attorney regarding accruals and disclosures for financial statements. She said Salt would likely be involved.

MPI/Pension Funding/Surplus Earnings

Mr. Schachter asked Ms. Devaney about her knowledge of MP1. She responded that she learned of it after the fact. Mr. Schachter asked Ms. Devaney if she was aware of the level of pension funding in 1996-1997. She responded that in the 1996-1997 time frame, she was not aware of the percentage of funding of the pension system or that it was not being fully funded. Mr. Schachter asked Ms. Devaney if she was aware of surplus earnings being used to fund the pension. She responded that she was not.

Corbett

Mr. Schachter asked Ms. Devaney about her knowledge regarding *Corbett*. She responded that she knew Bill Corbett because he was an investigator in the City Attorney's Office and said that he sued because of calculations of benefits to people covered under the system and retirees. She said that the suit alleged that the calculations used did not take into account sick time and other issues. Mr. Schachter asked Ms. Devaney if she was aware of the settlement terms and whether she was involved in determining whether the settlement was contingent. She responded that she did not know the terms of the settlement or the amount paid under the settlement, and was not involved in the determination of whether the settlement was contingent. She recalled having lunch with Ann Smith, an attorney for the Municipal Employees Association, in which Smith gave Ms. Devaney her opinion regarding *Corbett*, but Ms. Devaney did not remember what Smith said.

Gleason

Mr. Schachter asked Ms. Devaney to discuss her recollection of the *Gleason* litigation. She said she recalled that the *Gleason* litigation affected retirement benefits. She was unaware that the City failed to contribute in actuarially-required amounts and said she was not involved in the *Gleason* litigation.

NPO

Mr. Schachter asked Ms. Devaney about her involvement with the City's reporting of the Net Pension Obligation ("NPO"). Ms. Devaney responded that she was not involved.

Blue Ribbon Committee

Mr. Schachter asked Ms. Devaney about her involvement with the Blue Ribbon Committee ("BRC"). She recalled that it happened and remembered that she may have been involved with the legal issue of whether the BRC was or was not a Committee under the City Charter and thus whether the BRC would need to follow Brown Act noticing procedures. What she learned about the BRC, she learned during her campaign. She noted that April Boling, a member of the BRC, was the treasurer of her campaign.

Mr. Schachter asked Ms. Devaney whether she knew whether the findings of the BRC were delayed because of the Ballpark financing. She responded that she was not aware of delays regarding the findings of the BRC but was aware of the allegation that the findings were delayed until after the Ballpark Preliminary Official Statement ("POS"). She was not aware of the BRC findings but may have reviewed them during her campaign.

Labor Negotiations

Mr. Schachter asked Ms. Devaney about her involvement with labor negotiations. Ms. Devaney responded that she knew labor negotiations happened but that was all she could recall. Later in the interview, she stated that she learned about the labor union negotiation process and watched it unfold. She added that she only learned generally about presidential leave.

SDCERS Board's Conflicts of Interest

Mr. Schachter asked Ms. Devaney if she is aware of the allegations in the federal indictment. Ms. Devaney said she is aware of the allegations. She described those allegations as the fiduciaries to the retirement system, particularly City employees, violated § 1090 by taking affirmative acts which personally benefited them, thereby violating their fiduciary duties.

Mr. Schachter asked Ms. Devaney if she was ever concerned about the fact that the pension board consisted of City employees who voted on their own benefits. Ms. Devaney responded that she found it problematic that the pension board consisted of City employees who voted on their own benefits. She spoke about this conflict on the campaign trail.

Mr. Schachter asked Ms. Devaney if she recalled any discussion concerning that if Saathoff received such and such, he would do such and such for the pension board. Ms. Devaney responded that she had a general understanding that labor negotiation discussions would "involve consequences of actions taken" but had no recollection of discussion concerning that if Saathoff received such and such, he would do such and such for the pension board. Mr. Schachter asked Ms. Devaney if she had any recollection of discussions that pension system assets were declining or being under funded. She responded that she had no recollection of

discussions that the pension system assets were declining or being under funded. Mr. Schachter asked Ms. Devaney if she recalled discussion concerning that the SDCERS Board allowed decreased funding in exchange for increased benefits. She responded that she had no recollection of such discussion. Mr. Schachter asked Ms. Devaney if she recalled the SDCERS Board not taking action that the City wanted the Board to take. Ms. Devaney responded that she had no such recollection.

Pension Documents Discussed

Ms. Devaney was shown Exhibits 1-5:

- Exhibit 1 is a Closed Session Report of the City Council of March 18, 2002, with attached documentation;
- Exhibit 2 is a May 13, 2002 letter from Procopio Cory Hargreaves & Savitch LLP to Ms. Devaney re: "Income Tax Issues Arising When City of San Diego ("City") Employees Become Full-Time Union Representatives";
- Exhibit 3 is a Closed Session Report of the City Council, dated May 6, 2002, with attachments including handwritten notes and PowerPoint slides;
- Exhibit 4 is a June 23, 2002 email from Byron Wear to Cathy Lexin, Brian Maienschein, Donna Frye, George Stevens, Jim Madaffer, Ralph Inzunza, Scott Peters, Toni Atkins, Dick Murphy and copying Casey Gwinn, Elmer Heap, Leslie Devaney, Les Girard, Michael Uberuaga, and Lamont Ewell re: "Retirement Board Action"; and
- Exhibit 5 is a Closed Session Report of the City Council, dated July 9, 2002.

May 6, 2002 City Council Meeting

Regarding Exhibit 3, a Closed Session Report of the City Council, dated May 6, 2002, with attachments including handwritten notes and PowerPoint slides, Mr. Schachter asked whether the handwriting on the documents was hers. She responded that it is her handwriting but not her slides. Mr. Schachter asked Ms. Devaney when she first learned about presidential leave. She said that it was during the May 6, 2002 Closed Session that she first learned about presidential leave. She said presidential leave was a benefit only for the presidents of unions. She remembered a discussion about one union president who did not have presidential leave and that all others had it. Later in the interview, Ms. Devaney recalled that the one union president without presidential leave may have been Ron Saathoff. Mr. Schachter asked Ms. Devaney who made the slide presentation and who made the presentation to the Council. He also asked her to describe any conversation that took place during the presentation. She responded that she had no recollection about the slides, who made the presentation, or of any conversation that took place. She said that usually in labor negotiations, Cathy Lexin (Human Resources Director and SDCERS Board Trustee) made the presentation for the City Manager's Office. However, she

noted that Girard was present at the May 6 Closed Session. She said that since she was taking notes on the votes taking place, it suggested to her that Girard was involved in making the presentation to the Council. Mr. Schachter asked her what the "CD," "CD7," and "127" handwritten notations on the second page of Exhibit 3 mean. She responded that "CD" stands for "council district" and "CD7" is Councilman Madaffer's district. "127" stands for "Local 127."

The Trigger

Regarding Exhibit 4, a June 23, 2002 email from Byron Wear to Cathy Lexin, Brian Maienschein, Donna Frye, George Stevens, Jim Madaffer, Ralph Inzunza, Scott Peters, Toni Atkins, Dick Murphy and copying Casey Gwinn, Elmer Heap, Leslie Devaney, Les Girard, Michael Uberuaga, and Lamont Ewell re: "Retirement Board Action" and Exhibit 5, a Closed Session Report of the City Council of July 9, 2002, Mr. Schachter asked Mr. Devaney for her understanding of the word "trigger." She responded that she learned about the "trigger" on the campaign trail. She learned that decisions were made not to fund retirement because of balloon payments and that benefits were swapped out for funding under a decision by Jack McGrory. She tried to figure out what the "trigger" meant in 2004-2005. She was present for discussions regarding the trigger but only vaguely remembered tax implication questions arising regarding presidential leave. Mr. Schachter asked Ms. Devaney if she had any recollection of the "trigger" being discussed in Closed Session or of SDCERS not supporting a drop in the trigger. Ms. Devaney responded that she had no recollection of the "trigger" being discussed in Closed Session. She had no recollection regarding SDCERS not supporting a drop in the trigger to 75%.

Role of Ed Plank

Ms. Devaney was shown Exhibit 6, a November 18, 2002 email from Ed Plank to Cathy Lexin and Dan Kelley, copying Alison Glennon, Elmer Heap, Leslie Devaney, Loraine Chapin and Michael Rivo re: "Preparation of follow up memo on Retirement Process," attaching the November 18, 2002 minutes of the City Council. Mr. Schachter asked Ms. Devaney who Ed Plank was. Ms. Devaney responded that Ed Plank sat at the Council and was the coordinator for the docket on behalf of the City Manager's Office. He ran the City Manager's briefing before each upcoming Council meeting. He also coordinated presentations to the City Manager. Ms. Devaney said that she would often attend the presentations provided to the City Manager and answer questions the City Manager raised. Ms. Devaney stated that Plank sat behind the Manager at the Council meetings and assisted him.

Enterprise Funds

Ms. Devaney was shown Exhibit 7, a June 26, 2003 email from Terri Webster to Brian Maienschein, Casey Gwinn, Charles Lewis, Dick Murphy, Donna Frye, Ed Ryan, Frank Devaney, Jim Madaffer, Lamont Ewell, Les Girard, Leslie Devaney, Michael Uberuaga, Michael Zucchet, Pat Frazier, Ralph Inzunza, Russell Gold (Attorney, Luce Forward), Scott Peters, Toni Atkins, Timothy Pestotnik (Attorney, Luce Forward) re: "Retirement Payment." Mr. Schachter asked Ms. Devaney what Webster was talking about. She responded that she had "no idea." Ms. Devaney explained that an Enterprise Fund is a fund of a department that is self-funding. For water and sewer, there is an Enterprise Fund from taxes those departments receive, and the water and sewer departments use those taxes to sustain themselves. She recalled memos regarding the

conditions for using general funds for enterprise fund purposes and vice-versa. Ms. Devaney said that "under precedent and case law," the City could only use enterprise funds to fund the general fund if there is a causal link in the relationship. According to Ms. Devaney, the City can use the general fund for enterprise activities in an unrestricted fashion.

Staffing Concerns

Ms. Devaney was shown Exhibit 8, a draft letter dated October 6, 2004, to "Lamont" regarding concerns about the lack of competent legal counsel in the area of labor negotiations and pension issues. Mr. Schachter asked Ms. Devaney who wrote the letter. Ms. Devaney responded that she believed it may have been written by Lexin who was her client for labor negotiations. Lexin "always complained about everything." She vaguely remembered Lexin raising staffing concerns with her. Lexin helped select head deputies for various City Attorney units, and Ms. Devaney had a vague recollection of Lexin wanting to hand pick Lexin's unit head. Ms. Devaney noted that she left the City Attorney's Office a year prior to the writing of this letter.

Outside Counsel

Mr. Schachter asked Ms. Devaney about the City's policies regarding obtaining outside counsel. Ms. Devaney said that there was a difference of opinion as to whether the City Attorney's Office had to be involved. The conservative opinion said that Council approval was needed for certain amounts, which she pegged at amounts over \$20,000. In 2003, the City retained Luce Forward regarding unfunded liabilities owed by the pension system, but she was not aware of the retention at that time despite the fact that all outside counsel requests went through her. Mr. Schachter asked Ms. Devaney to explain how that could happen. She responded that that was likely because there was one exception to the process which was that Girard could hire outside counsel without Devaney's knowledge and Girard used Luce Forward a lot.

Wastewater

Proposition 218

Ms. Devaney was shown Exhibit 9, a December 8, 2000 email from Leslie Devaney to Elmer Heap and Keri Katz re: "Meeting with Mayor," and Exhibit 10, a memorandum of law from the City Attorney to George Loveland re: "The Application of Article XIID to Water, Sewer, and Storm Water Fees." Devaney recalled calling in Salt and asking about Proposition 218. Either she or Gwinn asked Salt to develop a seminar about 218 for the Assistant City Attorneys. Salt was involved with landscape maintenance districts regarding 218. Mr. Schachter asked Ms. Devaney if she had any involvement analyzing fees under 218. Ms. Devaney said she did not. Mr. Schachter asked Ms. Devaney who Elmer Heap was. She

responded that Elmer Heap was hired for a lead position in December 2000 and he gave good substantive information to the Mayor and Councilmember Scott Peters.

Ms. Devaney was shown Exhibits 11-16:

- Exhibit 11 is a Closed Session Report of the City Council, dated January 29, 2002.
- Exhibit 12 is a November 14, 2002 memo from the City Attorney to City Clerk Charles Abdelnour re: "Closed Session Agenda Items for November 19, 2002."
- Exhibit 13 is a November 28, 2002 email from Leslie Devaney to Leslie Devaney, Cathy Lexin, and Pat Frazier re: "cost of service study."
- Exhibit 14 is a January 21, 2003 email from Leslie Devaney to Kelly Salt, George Loveland, Pat Frazier, Richard Mendes, and John Kern re: "Cost of Service Study fo Wastewater user fees and charges."
- Exhibit 15 is a January 22, 2003 email from George Loveland to Richard Mendes and John Kern re: "Fwd: Cost of Service Study for Wastewater user fees and charges."
- Exhibit 16 is a November 14, 2002 memo from Mary Vattimo and Kelly Salt to the Honorable Mayor and City Council re: "Significant Exposure to Litigation: Metropolitan Wastewater Department's Compliance With Federal and State Loan and Grant Guidelines."

The COS and Closed Session

Mr. Schachter asked Ms. Devaney if she had any involvement in preparing Exhibit 16, a November 14, 2002 memo from Mary Vattimo and Kelly Salt to the Honorable Mayor and City Council re: "Significant Exposure to Litigation: Metropolitan Wastewater Department's Compliance With Federal and State Loan and Grant Guidelines." Ms. Devaney responded that she had seen the November 14, 2002 memo but did not recall it. Later in the interview, Mr. Schachter asked Ms. Devaney if she saw the issue of noncompliance with State requirements as a big issue when she received this memo from Salt. She said that at the time, she did not see it as a big issue. The Council saw it as a big issue and felt if the disparity was discussed in Open Session it would be difficult. She recalled a COS regarding sewer charges and vaguely recalled a Closed Session involving "energy" around a discrepancy of the cost of services not being proportionate to charges. Councilmember Frye told her of a concern regarding whether a vote could take place regarding the COS in Closed Session. Ms. Devaney challenged Girard on what was considered "anticipated litigation" and believed that items should usually be open for discussion in Open Session. She told Frye that she believed there should be public discussion regarding the COS but did not recall the COS being discussed in public. Mr. Schachter asked Ms. Devaney why the Closed Session happened on January 29, 2002, but Exhibit 16 was not finalized and sent to the Mayor and Council until November 2002. She admitted that from January 29, 2002, to November 2002 was a long time and vaguely recalled

people asking about the COS issue and about changing the sewer rates. She recalled a discussion in Closed Session about whether to talk about sewer rates and the COS in Open Session.

Mr. Schachter asked Ms. Devaney whether there was discussion about keeping the COS in Closed Session. She vaguely recalled an issue regarding the inappropriateness of discussing the COS in Closed Session. She remembered "lots of energy" over the COS and that the Council was upset about the results of the COS, particularly the discrepancy in charges among the residents and the businesses. Ms. Devaney said that the Council was concerned about the issue going to Open Session. She recalled that there was "energy" in Closed Session regarding "how awful Open Session would be."

Mr. Schachter asked Ms. Devaney to describe in particular what was said during the Closed Session in which the COS was discussed. Ms. Devaney said that while she cannot remember, she would not tell if she did because it is protected by privilege. She added that "Aguirre would prosecute people for telling what happened in Closed Session." Mr. Schachter explained that the privilege has been waived. Mr. Schachter asked Ms. Devaney if she recalled that the COS was listed for discussion on an agenda for a Closed Session and then the Closed Session was cancelled. She said she did not recall but stated that items were pulled from agendas regularly.

Mr. Schachter asked Ms. Devaney if she recalled any member of the Council saying "let them sue us" at any time when she was present. She remembered the Council saying "let them sue us" "all the time" and felt it was probably said during the January 29, 2002 Closed Session as well. The Council did not want to be intimidated by suit. Mr. Schachter asked Ms. Devaney if she recalled the November 19, 2002 Closed Session being cancelled. She did not.

Discussions with Salt and Katz Regarding the COS

Mr. Schachter asked Ms. Devaney if she recalled discussing the status of the COS with Salt. She vaguely recalled that in January 2003, she asked Salt the status of the COS. Ms. Devaney recalled that John Kern, the Mayor's Chief of Staff, called her about the COS and she gathered information from Salt in response to his call. Kern likely asked her if the need to implement the COS was documented in writing.

Ms. Devaney was shown Exhibit 17, a March 6, 2003 email from Dennis Kahlie to Christine Ruess, Kelly Salt, and Eric Adachi re: "Cost of service study-questions," attaching a March 6, 2003 email from Dennis Kahlie to Keri Katz, Leslie Devaney, Richard Mendes, Scott Tulloch, and Bill Hanley re: "Cost of service study-questions", attaching a March 6, 2003 memo from Dennis Kahlie to Keri Katz re: "Information Requested Relative to Utility Cost of Service Studies." Ms. Devaney stated that Keri Katz is head of the public works department. Katz's unit includes Financing Services and Katz was Salt's supervisor. Mr. Schachter asked who the "Richard" is who is noted in the Exhibit. She said that "Richard" is Richard Mendes. She recalled that every Friday, Ms. Devaney had meetings with Anita Noone (Assistant City Attorney) with all of the attorney heads to apprise everyone of top issues. Mr. Schachter asked Ms. Devaney if she recalled speaking with Katz about the COS. She responded that she did not recall speaking with Katz about the COS and did not recall reviewing the COS. Mr. Schachter asked Ms. Devaney how she first learned about the COS. Ms. Devaney said that she learned

from Salt what the COS was and why a nexus was needed between the services performed and taxes paid. Salt told her that the COS got out of "sync" quickly and therefore it was necessary to regularly tweak it.

Why the Rates were not Changed

Mr. Schachter asked Ms. Devaney why the sewer rates were not changed. She said that she did not know.

Kelco

Mr. Schachter asked Ms. Devaney if she recalled Kelco being involved with the rate issue. Ms. Devaney recalled discussion regarding proportionate use and residential versus commercial users but did not recall Kelco being involved.

Conclusion

Mr. Schachter asked Ms. Devaney if she has witnessed or heard of any employee doing anything unethical, improper or illegal, to which Ms. Devaney replied "no." Mr. Schachter requested that if Ms. Devaney wished to change her answers or provide us with any new information, she should contact us.

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